



SECURITIES AND EXCHANGE COMMISSION
[Release No. 34-91258; File No. SR-FINRA-2020-041]

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Instituting Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change to Adopt FINRA Rule 4111 (Restricted Firm Obligations) and FINRA Rule 9561 (Procedures for Regulating Activities Under Rule 4111)

March 4, 2021

I. Introduction

On November 16, 2020, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change SR-FINRA-2020-041 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”)¹ and Rule 19b-4² thereunder to address the risks that can be posed to investors and the broader market by broker-dealers that have a history of misconduct. The proposed rule change was published for public comment in the Federal Register on December 4, 2020.³ On January 12, 2021, FINRA consented to extend, until March 4, 2021, the time period in which the Commission must approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change.⁴ The Commission is publishing this order pursuant to Section 19(b)(2)(B) of the Exchange Act⁵ to institute proceedings to determine whether to approve or disapprove the proposed rule change.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Exchange Act Release No. 90527 (Nov. 27, 2020), 85 FR 78540 (Dec. 4, 2020) (File No. SR-FINRA-2020-041) (“Notice”).

⁴ See letter from Michael Garawski, Associate General Counsel, OGC Regulatory Practice and Policy, FINRA, to Daniel Fisher, Branch Chief, Division of Trading and Markets, Commission, dated January 12, 2021.

⁵ 15 U.S.C. 78s(b)(2)(B).

II. Description of the Proposed Rule Change

The proposed rule change would: (1) adopt FINRA Rule 4111 (Restricted Firm Obligations) to require member firms that are identified as “Restricted Firms” to maintain a deposit in a segregated account with withdrawals requiring FINRA’s approval, adhere to specified conditions or restrictions, or comply with a combination of such obligations; and (2) adopt FINRA Rule 9561 (Procedures for Regulating Activities Under Rule 4111), and amend FINRA Rule 9559 (Hearing Procedures for Expedited Proceedings Under the Rule 9550 Series), to create a new expedited proceeding to implement proposed Rule 4111.⁶

Proposed Rule 4111 (Restricted Firm Obligations)

Proposed Rule 4111 would establish numeric thresholds based on firm-level and individual-level disclosure events to identify member firms with a significantly higher level of risk-related disclosures as compared to similarly-sized peers.⁷ Following a multi-step process of evaluating a member firm, FINRA’s Department of Member Regulation (“Department”) would be permitted to impose on member firms it determines pose a high risk to the investing public a “Restricted Deposit Requirement,”⁸ conditions or restrictions on the member firm’s operations that are necessary or appropriate to protect investors and the public interest, or both.⁹

FINRA would conduct the process annually for each member firm, determining whether it should be designated (or re-designated) as a Restricted Firm and whether it should be subject to any obligations.¹⁰ Each member firm that is preliminarily identified based on its firm-level and individual-level disclosure events would have several ways to affect outcomes during

⁶ See Notice at 78541-78550.

⁷ See Notice at 78541.

⁸ See proposed Rule 4111(i)(15) (defining “Restricted Deposit Requirement”).

⁹ See Notice at 78542.

¹⁰ Id.

subsequent steps in the evaluative process, including a one-time opportunity to terminate registered representatives with relevant disclosure events so as to no longer trigger the numeric thresholds.¹¹ The member firm would also be able to explain to the Department why it should not be subject to a Restricted Deposit Requirement or propose alternatives that would still accomplish FINRA's goal of protecting investors, and could request a hearing before a FINRA Hearing Officer in an expedited proceeding to challenge a Department determination.¹²

General (Proposed Rule 4111(a))

Under the proposal, any member firm that is designated by the Department as a Restricted Firm would be required to establish a Restricted Deposit Account¹³ and maintain within that account deposits of cash or qualified securities with an aggregate value that is not less than the member firm's Restricted Deposit Requirement, except in certain identified situations.¹⁴

¹¹ Id.

¹² Id.

¹³ See proposed Rule 4111(i)(14)(defining "Restricted Deposit Account"). Proposed Rule 4111(i)(14) would require that any Restricted Deposit Account that is established must be in the name of the member firm, at a bank or the member firm's clearing firm. The account must be subject to an agreement in which the bank or the clearing firm agrees: not to permit withdrawals from the account absent FINRA's prior written consent; to keep the account separate from any other accounts maintained by the member firm with the bank or clearing firm; that the cash or qualified securities on deposit will not be used directly or indirectly as security for a loan to the member firm by the bank or the clearing firm, and will not be subject to any set-off, right, charge, security interest, lien, or claim of any kind in favor of the bank, clearing firm or any person claiming through the bank or clearing firm; that if the member firm becomes a former member, the Restricted Deposit Requirement in the account must be maintained, and withdrawals will not be permitted without FINRA's prior written consent; that FINRA is a third-party beneficiary to the agreement; and that the agreement may not be amended without FINRA's prior written consent. In addition, the account could not be subject to any right, charge, security interest, lien, or claim of any kind granted by the member.

In the event of a liquidation of a Restricted Firm, funds or securities on deposit in the Restricted Deposit Account would be additional financial resources available for the Restricted Firm's trustee to distribute to those with claims against the Restricted Firm.

¹⁴ See Notice at 78542. FINRA is also proposing to include Supplementary Material .01 to proposed Rule 4111 to clarify that due to withdrawal restrictions from a Restricted Deposit Account, deposits in such an account cannot be readily converted to cash and therefore shall be

Restricted Firms could also be subject to conditions or restrictions on their operations,¹⁵ as determined by the Department to be necessary or appropriate to protect investors and the public interest.¹⁶

Annual Calculation by FINRA of the Preliminary Criteria for Identification (Proposed Rule 4111(b))

The Department would begin a member firm's Rule 4111 review process by calculating specified "Preliminary Identification Metrics" for that firm across six categories of events or conditions, collectively defined as the "Disclosure Event and Expelled Firm Association Categories."¹⁷ These six categories include risk events, covering adjudicated and pending actions against firms and their registered representatives, along with metrics addressing registered representatives' termination and internal review history, and their association with former member firms that were previously expelled by FINRA.¹⁸ FINRA would use a formula to identify whether the firm has exceeded certain established thresholds,¹⁹ set based on the firm's

deducted from the member's net capital under Exchange Act Rule 15c3-1 and FINRA Rule 4110. See Notice at 78548.

¹⁵ FINRA has also proposed adopting Supplementary Material .03 to proposed Rule 4111 to provide member firms with a non-exhaustive list of examples of conditions and restrictions that the Department could impose on Restricted Firms. See Notice at 78458.

¹⁶ See Notice at 78452. FINRA has also proposed adding Supplementary Material .02 to proposed Rule 4111 to clarify that nothing in proposed Rule 4111 would alter a member firm's obligations under Rule 1017 (Application for Approval of Change in Ownership, Control, or Business Operations), and the need to submit continuing membership applications as necessary. See Notice at 78458.

¹⁷ See proposed Rule 4111(i)(4) (defining "Disclosure Event and Expelled Firm Association Categories").

¹⁸ See Notice at 78542.

¹⁹ See proposed Rule 4111(i)(11) (defining "Preliminary Identification Metrics Thresholds").

size,²⁰ across the six categories, starting by determining the sum of the pertinent disclosure events or, for the Expelled Firm Association category, the sum of the Registered Persons Associated with Previously Expelled Firms as of the calculation date.²¹ Based on this calculation, the Department would determine whether the particular member firm meets the “Preliminary Criteria for Identification.”²² FINRA has indicated that it developed the criteria and thresholds for identification with the intent to be replicable and transparent to both FINRA and affected member firms; employ the most complete and accurate data available to FINRA; be objective; account for different firm sizes and business profiles; and target sales practice concerns.²³

Initial Department Evaluation (Proposed Rule 4111(c)(1))

The Department would then evaluate whether a member firm that has met the Preliminary Criteria for Identification warrants further review under Rule 4111.²⁴ This would include consideration of: whether non-high-risk disclosure events or other conditions should not have been included within the initial calculation of the firm’s Preliminary Identification Metric computations (e.g., because, for example, they were not sales-practice related, or include duplicative events involving the same customer and the same matter, or events involving compliance concerns best addressed by a different regulatory response by FINRA);²⁵ whether the disclosure events pose risks to investors or market integrity, as opposed to violations of

²⁰ Specifically, member firms would be divided into seven firm size categories based on size, ranging from firms with 1-4 “Registered Persons In-Scope,” defined in proposed Rule 4111(i)(13), to 500 or more Registered Persons In-Scope. See Notice at 78544.

²¹ See Notice at 78543.

²² See proposed Rule 4111(i)(9) (defining “Preliminary Criteria for Identification”).

²³ See Notice at 78542.

²⁴ See Notice at 78544.

²⁵ Id.

procedural rules;²⁶ and whether the member firm has already addressed the concerns signaled by the disclosure events or conditions, or has altered its business operations such that the threshold calculation no longer reflects the firm's current risk profile.²⁷ The Department would then either determine that further review is necessary and continue the Rule 4111 process, or, if the Department concluded that no further review is warranted, close out that member firm's Rule 4111 process for the year without imposing any restrictions or obligations.²⁸

FINRA originally stated that it would conduct this annual evaluation on the same month and day each year where that date was a business day, and that if that date were a weekend date or federal holiday, the evaluation would shift to the next business day.²⁹ FINRA has since stated that it would announce the date of the first annual evaluation ("Evaluation Date") no less than 120 calendar days prior to the first Evaluation Date.³⁰ Subsequent Evaluation Dates would be on the same month and day each year, whether that date certain falls on a business day, a weekend day, or a holiday.³¹

One-Time Opportunity to Reduce Staffing Levels (Proposed Rule 4111(c)(2))

If the Department determines that a member firm warrants further review under Rule 4111, and such member firm is meeting the Preliminary Criteria for Identification for the first time, the member firm would have a one-time opportunity to reduce its staffing levels to no

²⁶ See Notice at 78544-45.

²⁷ See Notice at 78545.

²⁸ Id.

²⁹ See Notice at 78544.

³⁰ Id.

³¹ See letter from Michael Garawski, Associate General Counsel, Office of General Counsel, FINRA, to Vanessa Countryman, Secretary, Commission, dated March 4, 2021 ("FINRA March 4 Letter"). The FINRA March 4 Letter is available at the Commission's website at <https://www.sec.gov/comments/sr-finra-2020-041/srfinra2020041.htm>.

longer meet these criteria, within 30 business days after being informed by the Department.³²

The member firm would need to identify the terminated individuals to the Department, and would be prohibited from rehiring any of those terminated persons, in any capacity, for one year.³³

Determination of a Maximum Restricted Deposit Requirement (Proposed Rule 4111(i)(15))

For firms still meeting the Preliminary Criteria for Identification, the Department would then determine the firm's maximum Restricted Deposit Requirement,³⁴ and the member firm would proceed to a "Consultation" with the Department.³⁵ FINRA states that the Department would seek to tailor a firm's maximum Restricted Deposit Requirement amount to its size, operations and financial conditions, and determine the member firm's maximum Restricted Deposit Requirement consistent with the objectives of the rule, while not significantly undermining the firm's continued financial stability and operational capability as an ongoing enterprise over the next 12 months.³⁶

³² See Notice at 78544.

³³ Id. If the member firm reduces its staffing levels, and the Department then determines that the member firm no longer meets the Preliminary Criteria for Identification, the Department would close out the firm's Rule 4111 process for the year without seeking to impose any restrictions or obligations on that firm. However, if the Department determines that the member firm still meets the Preliminary Criteria for Identification (or if the member firm did not opt to reduce staffing levels) the Department would determine the firm's maximum Restricted Deposit Requirement, and the member firm would proceed to a "Consultation" with the Department.

³⁴ The term "maximum" is used to indicate that a firm's maximum Restricted Deposit Requirement will be the figure FINRA declares to the firm is the highest deposit requirement it may be subject to during that year's Rule 4111 process. As discussed below, firms could then seek to demonstrate to FINRA why a lower deposit requirement would be more appropriate, during the Consultation. See FINRA March 4 Letter supra n.31.

³⁵ See Notice at 78545.

³⁶ Id. The proposed factors that the Department would consider when determining a maximum Restricted Deposit Requirement include revenues, net capital, assets, expenses, and liabilities, the firm's operations and activities, number of registered persons, the nature of the disclosure events included in the numeric thresholds, insurance coverage for customer arbitration

Consultation (Proposed Rule 4111(d))

During the Consultation, the Department would give the member firm an opportunity to demonstrate why it does not meet the Preliminary Criteria for Identification, why it should not be designated as a Restricted Firm, and why it should not be subject to the maximum Restricted Deposit Requirement.³⁷

A member firm may overcome the presumption that it should be designated as a Restricted Firm by clearly demonstrating that the Department's calculation is inaccurate because, among other things, it considered events that should not have been included.³⁸ A member firm also may overcome the presumption that it should be subject to the maximum Restricted Deposit Requirement by clearly demonstrating that such an amount would cause significant undue financial hardship, and that a lesser deposit requirement would satisfy the objectives of Rule 4111 to impose obligations on those firms identified as presenting a higher risk to investors; or that other operational conditions and restrictions on the member and its associated persons would sufficiently protect investors and the public interest.³⁹ To the extent a member firm seeks to claim undue financial hardship, it would bear the burden of supporting that claim with documents and information.⁴⁰

Department Decision and Notice (Proposed Rule 4111(e)); No Stays

awards or settlements concerns raised during FINRA exams, and the amount of any of the firm's or its associated persons' "Covered Pending Arbitration Claims" or unpaid arbitration awards. See proposed FINRA Rule 4111(i)(15)(A).

³⁷ See Notice at 78545.

³⁸ Id. These would include, for example, events that are duplicative, involving the same customer and the same matter, or are not sales-practice related.

³⁹ Id. Proposed Rule 4111(d)(3) provides guidance to member firms on what information the Department would consider during the Consultation, and guidance on how to attempt to overcome the two rebuttable presumptions (that the member firm should be designated as a Restricted Firm, and that it should be subject to the maximum Restricted Deposit Requirement). See Notice at 78546.

⁴⁰ See Notice at 78545.

After the Consultation, the Department would be required to render a decision, pursuant to one of three paths: (1) if the Department determines that the member firm has rebutted the presumption that it should be designated a Restricted Firm, the Department would not designate the firm as a Restricted Firm that year; (2) if the Department determines that the member firm has not rebutted the presumption that it should be designated as a Restricted Firm, but has rebutted the presumption that it must maintain the maximum Restricted Deposit Requirement, the Department would designate the member firm as a Restricted Firm, but would either impose no Restricted Deposit Requirement on the member firm, or require it to promptly establish a Restricted Deposit Account, and deposit and maintain in that account a lower Restricted Deposit Requirement in such dollar amount as the Department deems necessary or appropriate; and would require the member firm to implement and maintain specified conditions or restrictions on the operations and activities of the member firm and its associated persons, as necessary or appropriate, to address the concerns identified by the Department, and protect investors and the public interest; or (3) if the Department determines that the member firm has rebutted neither presumption, the Department would designate the member firm as a Restricted Firm, require it to promptly establish a Restricted Deposit Account, deposit and maintain in that account the maximum Restricted Deposit Requirement, and implement and maintain specified conditions or restrictions on the firm's operations and activities, and those of its associated persons, as necessary or appropriate to address the concerns identified by the Department and protect investors and the public interest.⁴¹ The Department would provide the member firm with written notice of its decision no later than 30 days from its latest scheduling letter provided to the member firm, stating any obligations to be imposed, and the ability of it to request a hearing with the Office of Hearing Officers in an expedited proceeding.⁴²

⁴¹ See Notice at 78546.

⁴² Id. As noted below, any request for a hearing would not stay the effectiveness of the Department's decision, but would temporarily lower the necessary Required Deposit

Continuation or Termination of Restricted Firm Obligations (Proposed Rule 4111(f))

During the Department's annual Rule 4111 review, a Restricted Firm could seek to terminate or modify any obligations that continue to be imposed.⁴³ Restricted Firms would only be permitted to seek this result during their annual Consultation, and any ensuing expedited proceedings after a Department decision; no interim termination or modification of any obligations would be permitted.⁴⁴ A Restricted Firm would not be permitted to withdraw any portion of its Restricted Deposit Requirement, or to seek to terminate or modify any other conditions or obligations that have been imposed, without the prior written consent of the Department.⁴⁵

Where the Department determines in one year that a member firm is a Restricted Firm, but in the following year(s) determines that the member firm or former member firm⁴⁶ either does not meet the Preliminary Criteria for Identification or should not be designated as a Restricted Firm, the member firm or former member firm would no longer be subject to any obligations previously imposed under proposed Rule 4111.⁴⁷ There would be one exception: a former Restricted Firm would not be permitted to withdraw any portion of its Restricted Deposit

Requirement for that member firm until the Office of Hearing Officers, or the National Adjudicatory Council ("NAC") issues a final written decision, unless that firm was already operating as a Restricted Firm based on a prior year's Department decision.

⁴³ See Notice at 78547. See also proposed Rule 4111(f)(1).

⁴⁴ See Notice at 78547.

⁴⁵ Id. There would be a presumption that the Department shall deny an application by a member firm or former member firm that is currently designated as a Restricted Firm to withdraw all or any portion of its Restricted Deposit Requirement.

⁴⁶ See Notice at 78547. See also proposed Rule 4111(i)(7) (defining "Former Member").

⁴⁷ See Notice at 78547.

Requirement without submitting an application in the manner specified under Rule 4111(f)(3)(A), and obtaining the Department's prior written consent for the withdrawal.⁴⁸

In this situation, the Department would be subject to a presumption that it shall approve an application for withdrawal if the member firm, its associated persons, or the former member firm have no Covered Pending Arbitration Claims⁴⁹ or unpaid arbitration awards.⁵⁰ The rule would also establish presumptions that the Department shall: (a) deny an application for withdrawal if the member firm, the member firm's associated persons who are owners or control persons, or the former member have any Covered Pending Arbitration Claims or unpaid arbitration awards, or if the member's associated persons have any Covered Pending Arbitration Claims or unpaid arbitration awards relating to arbitrations that involved conduct or alleged conduct that occurred while associated with the member; but (b) approve an application by a former member for withdrawal if the former member commits in the manner specified by the Department to use the amount it seeks to withdraw from its Restricted Deposit to pay the former member's specified unpaid arbitration awards.⁵¹

Books and Records (Proposed Rule 4111(g))

Member firms would also be obligated to maintain books and records that evidence its compliance with Rule 4111 and any Restricted Deposit Requirement or other conditions or

⁴⁸ Id. The Department would be required to issue a notice of its decision within 30 days from the date it receives the relevant application.

⁴⁹ See proposed Rule 4111(i)(2) (defining Covered Pending Arbitration Claim as an investment-related, consumer initiated claim filed against the member or its associated persons in any arbitration forum that is unresolved; and whose claim amount (individually or, if there is more than one claim, in the aggregate) exceeds the member firm's excess net capital).

⁵⁰ See Notice at 78547.

⁵¹ Id. Proposed Rule 4111(f)(3) provides that the Covered Pending Arbitration Claims and unpaid arbitration awards of a member firm's associated persons are pertinent to an application for a withdrawal from the Restricted Deposit Requirement.

restrictions imposed under that rule, that the member firm would need to provide to the Department upon request.⁵²

Planned Review of Proposed Rule 4111

FINRA has indicated it intends to conduct a review of proposed Rule 4111 after gaining sufficient experience under Rule 4111 following its effective date.⁵³ FINRA has indicated that it expects to review, among other items, whether the Preliminary Identification Metrics Thresholds remain targeted and effective at identifying member firms that pose higher risks.⁵⁴

Proposed Rule 9561 (Procedures for Regulating Activities under Rule 4111) and Amendments to Rule 9559 to Implement the Requirements of Proposed Rule 4111

FINRA is proposing Rule 9561 to establish new expedited proceedings that would: (a) provide member firms an opportunity to challenge any requirements the Department has imposed, including any Restricted Deposit Requirements, by requesting a prompt review of the Department's decision in the Rule 4111 process;⁵⁵ and (b) address a member firm's failure to comply with any requirements imposed under Rule 4111.⁵⁶

Notices Under Proposed Rule 4111 (Proposed Rule 9561(a))

Under proposed Rule 9561(a)(1), the Department would be obligated to serve a notice of its decision following the Rule 4111 process that provides the specific grounds and factual basis

⁵² See Notice at 78548.

⁵³ Id.

⁵⁴ Id.

⁵⁵ Id. Proposed Rule 9561(a)(1) would define the "Rule 4111 Requirements" to mean the requirements, conditions, or restrictions imposed by a Department determination under proposed Rule 4111. See Notice at 78548.

⁵⁶ See Notice at 78549.

for the Department's action; states when the action will take effect; informs the member firm that it may request a hearing in an expedited proceeding within seven days after service of the notice; and explains the Hearing Officer's authority.⁵⁷ The proposed rule would also provide that, if a member firm does not request a hearing, the decision will constitute final FINRA action.⁵⁸

Any of the Rule 4111 Requirements imposed in the Department's decision would be immediately effective.⁵⁹ In general, a request for a hearing would not stay those requirements.⁶⁰ There would be one exception: when a member firm requests review of a Department determination to impose a Restricted Deposit Requirement on the member, the firm would be required to deposit the lesser of 25% of its Restricted Deposit Requirement or 25% of its average excess net capital over the prior year, while the expedited proceeding was pending.⁶¹ This exception would not be available for a member firm that has been re-designated as a Restricted Firm, and is already subject to a previously imposed Restricted Deposit Requirement, which it will need to maintain in full until the Office of Hearing Officers or NAC issues a written decision.⁶²

Notice for Failure to Comply with the Proposed Rule 4111 Requirements (Proposed Rule 9561(b))

After receiving authorization from FINRA's chief executive officer ("CEO"), or such other executive officer as the CEO may designate, the Department would be authorized to serve

⁵⁷ Id.

⁵⁸ See Notice at 78548-49.

⁵⁹ See Notice at 78549.

⁶⁰ Id.

⁶¹ Id.

⁶² See Notice at 78546. Thereafter, if a member firm is not in compliance with its Restricted Deposit Requirement or with any conditions or restrictions imposed under proposed Rule 4111, FINRA would be authorized to issue a notice pursuant to proposed Rule 9561 directing a member firm to suspend all or a portion of its business. See Notice at 78548.

a notice stating that the member firm's failure to comply with the Rule 4111 Requirements, within seven days of service of the notice, will result in a suspension or cancellation of membership.⁶³ Proposed Rule 9561(b) would establish an expedited proceeding to review the Department's decision to issue a suspension or cancellation notice to a member firm for its failure to comply with requirements of Rule 4111. If a member firm does not request a hearing, the suspension or cancellation will become effective seven days after service of the notice.⁶⁴

Hearings (Proposed Amendments to the Hearing Procedures Rule)

If a member firm requests a hearing under proposed Rule 9561, the hearing would be subject to Rule 9559 (Hearing Procedures for Expedited Proceedings Under the Rule 9550 Series). FINRA is proposing several amendments to Rule 9559 that would be specific to hearings requested pursuant to proposed Rule 9561.⁶⁵

Effective Date

⁶³ See Notice at 78549. The notice must identify the requirements with which the member firm is alleged to have not complied; specify the facts involved in the alleged failure; state when the action will take effect; explain what the member firm must do to avoid the suspension or cancellation; inform the member firm that it may file a request for a hearing in an expedited proceeding within seven days after service of the notice under Rule 9559; and explain the Hearing Officer's authority.

⁶⁴ *Id.* After a suspension has been imposed, a member firm could file a request under Rule 9561(b) to terminate the suspension on the ground of full compliance with the notice or decision, and the head of the Department would be permitted to grant relief for good cause shown.

⁶⁵ *Id.* Specifically, FINRA has proposed to (a) amend Rule 9559(d) and (n) to establish the authority of a Hearing Officer in expedited proceedings under Rule 9561; (b) amend Rule 9559(f) to set out timing requirements for hearings conducted under Rules 9561(a) and (b); and (c) amend Rule 9559(p)(6) to account for the obligations that may be imposed under proposed Rule 4111 within the content requirements of any decision issued by a Hearing Officer under the Rule 9550 Series. See proposed amended Rules 9559(d), (f), (n), and (p)(6). Additionally, FINRA has noted that in expedited proceedings conducted under proposed Rule 9561(a) to review a Department determination under the Restricted Firm Obligations Rule, a member firm would be permitted to try to demonstrate that the Department incorrectly included disclosure events when calculating whether the member firm meets the Preliminary Criteria for Identification. However, the member firm attempting to do so would not be permitted to collaterally attack the underlying merits of the final actions underlying the disclosure events. See Notice at 78550.

If the proposed rule is approved by the Commission, FINRA has indicated it will announce an effective date for the proposed rule in a Regulatory Notice to be published no later than 60 days following the Commission approval.⁶⁶ FINRA originally stated that the effective date would be no later than 60 days following publication of the Regulatory Notice announcing Commission approval.⁶⁷ However, FINRA has since extended the timeline of the effective date to 180 days after the Regulatory Notice announcing Commission approval.⁶⁸

III. Proceedings to Determine Whether to Approve or Disapprove File No. SR-FINRA-2020-041 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings to further consider the proposed rule change and the issues raised by commenters.

Specifically, the Commission is providing notice of the following grounds for possible disapproval under consideration:

- Whether FINRA has demonstrated how its proposed rule change is consistent with Section 15A(b)(6) of the Exchange Act, which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.⁶⁹

Under the Commission's Rules of Practice, the "burden to demonstrate that a proposed rule change is consistent with the [Exchange Act] and the rules and regulations issued thereunder...is on the [SRO] that proposed the rule change."⁷⁰ The description of a proposed

⁶⁶ See Notice at 78550.

⁶⁷ Id.

⁶⁸ See FINRA March 4 Letter supra n.31.

⁶⁹ 15 U.S.C. 78o-3(b)(6).

⁷⁰ Rule 700(b)(3), Commission Rules of Practice, 17 CFR 201.700(b)(3).

rule change, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding,⁷¹ and any failure of an SRO to provide this information may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Exchange Act and the applicable rules and regulations.⁷²

For the reasons discussed above, the Commission believes it is appropriate to institute proceedings pursuant to Section 19(b)(2)(B) of the Exchange Act to allow for additional consideration of the issues raised by the proposed rule change as it determines whether the proposed rule change should be approved or disapproved.⁷³

IV. Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the proposed rule change. In particular, the Commission invites the written views of interested persons concerning whether the proposed rule change is consistent with the Exchange Act and the rules thereunder.

Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.⁷⁴

⁷¹ See id.

⁷² See id.

⁷³ 15 U.S.C. 78s(b)(2)(B).

⁷⁴ Section 19(b)(2) of the Exchange Act, as amended by the Securities Acts Amendments of 1975, Pub. L. 94-29, 89 Stat. 97 (1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Acts Amendments of 1975, Report of the Senate Committee on Banking, Housing and Urban Affairs to Accompany S. 249, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

Interested persons are invited to submit written data, views, and arguments regarding whether the proposed rule change should be approved or disapproved by [insert date 14 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 21 days from publication in the Federal Register]. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File No. SR-FINRA-2020-041 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File No. SR-FINRA-2020-041. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change, that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC, 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File No. SR- FINRA-2020-041 and should be submitted on or before [insert date 14 days from publication in the Federal Register]. If comments are received, any rebuttal comments should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁷⁵

J. Matthew DeLesDernier
Assistant Secretary

[FR Doc. 2021-04912 Filed: 3/9/2021 8:45 am; Publication Date: 3/10/2021]

⁷⁵ 17 CFR 200.30-3(a)(12); 17 CFR 200.30-3(a)(57).